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INTRODUCTION

The DHS Office of Internal Audit (OIA) performed a limited scope audit of the Department's Fiscal Year 2005 Year End Closing transactions and processes (October 1, 2004-September 30, 2005).

The objectives of our audit were:

1. Review a sample test of accounts payable and encumbrance transactions
2. Review the child support accrual methodology for estimated payables or receivables

This audit was limited in scope and nature and, therefore, was not conducted in accordance with all Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

SCOPE

The scope of our audit included obtaining and reviewing appropriate records and documents, as we considered necessary to satisfy our objectives. Audit work was performed primarily between November 14, 2005 and February 1, 2006.

For objective one, we obtained the lists of accounts payable and encumbrances established at the 2004-2005 fiscal year-end. The total amount of accounts payable (Account #1215) established was \$90,991,613.89 and the amount of encumbrances was \$15,753,750.63. We sampled 11 accounts payable and reviewed the supporting documentation to determine if the payable was proper and if the amount was reasonable. We reviewed one encumbrance to determine if Accounting ensured that the transaction met the criteria to qualify as an encumbrance. We reviewed the unliquidated balances from the prior year and their disposition. We reviewed vendor payroll accounts payable

to ensure that old year charges from split payrolls were charged back to the old fiscal year.

For objective two, we reviewed prior year child support accrual work papers to obtain an understanding of the prior year accrual process. We met with Office of Child Support (OCS) management to obtain an understanding of the current year's accrual methodology used to prepare the child support accrual estimate, including their review of key factors and assumptions used to compute the estimate. We obtained an understanding of the methods used by OCS to ensure the accuracy of the accrual numbers including documenting any changes to the Michigan Child Support Enforcement System (MiCSES) Data Warehouse data transfer process and reconciliation. We reviewed the query logic used to pull data used in the estimate and tested sample cases from the MiCSES Data Warehouse to the source system (MiCSES) for completeness and accuracy.

EXECUTIVE SUMMARY

Based on our review, we determined that payable and encumbrance transactions processed as part of the FY05 year-end closing by the Bureau of Accounting appeared to be proper and were supported by adequate documentation except for the Foster Care payroll estimation. We provided one recommendation related to objective one.

We determined that the methodology used by OCS for calculating estimated payables and receivables for the FY05 child support accrual appears to be adequate. We also determined, with reasonable assurance, that the data used to calculate the child support accrual appears to be accurate and complete. We provided two repeat recommendations related to objective two, regarding controls that could be implemented to help strengthen the child support accrual estimation in the future. Implementing these recommendations would also help DHS comply with a material weakness related to maintaining sound

internal control over the child support accrual identified in a prior Office of the Auditor General audit of the child support accrual methodology (Report 43-101-99F).

AGENCY RESPONSE:

The Bureau of Accounting responded in an email dated April 14, 2006 that they partially agree with the Accounts Payable recommendation. They stated that they rely on responsible program office staff to provide this information. For FY2005, this information was not made available to the Bureau of Accounting in time to meet DMB year end closing deadlines. In the absence of this information, the Bureau of Accounting utilized the previous year's estimate to ensure compliance with the State of Michigan Financial Guide, which requires utilization of the most recent information available in the estimation of the accounts payable amount. The Bureau of Accounting further stated that they are incorporating improved communication measures with the responsible program area for the FY2006 year end closing.

The Office of Child Support did not respond to our draft report.

FINDINGS AND RECOMMENDATIONS:

Accounts Payable

1. The Bureau of Accounting did not use the most recent information available to estimate the Foster Care accounts payable for payments made in FY 2006 that were for expenditures attributable to FY 2005. The Bureau of Accounting used the same estimate that was used at the end of the prior fiscal, although 11 months of new-year data was available.

The State of Michigan Financial Guide, Chapter 14, Section 100 states that an accounts payable may be established on an estimated basis, however, the concept of matching must be considered. Matching of revenue and expenditures would have been improved if the most recent data had been used.

WE RECOMMEND that the Bureau of Accounting use the most recent information available when estimating accounts payable.

Child Support Accrual Methodology

2. OCS should document the methodology followed to calculate the annual child support accrual estimate.

OCS had final data and accrual calculation numbers available, however, they had not documented the methodology used to calculate the accrual. Documenting the methodology would provide a history of the accrual process and estimation and a point of reference to ensure consistent treatment in future periods. Documenting the methodology followed also helps to ensure the process could be performed in the absence of the individuals who currently perform the accrual calculation/estimate. Because OCS has not documented the methodology, they do not have a history of how the estimate was performed or has changed over the years.

WE RECOMMEND that OCS document the methodology followed to calculate the annual child support accrual.

Review of Key Factors and Assumptions

3. OCS should formally document their review of key factors and assumptions that support the annual child support accrual estimate.

Although we believe that key factors and assumptions were reviewed prior to the FY05 accrual being calculated, OCS did not document which factors and assumptions were reviewed. Examples of key factors or assumptions that may be considered include changes in the child support program that affect arrearage balances, changes made to the information system that processes child support payments that may affect case level information, etc. Formal documentation would help to ensure the integrity of the process and formalize an understanding of the exact factors and assumptions considered in the review process.

WE RECOMMEND that OCS formally document any key factors and assumptions they review prior to calculating the annual child support accrual.